

104TH CONGRESS  
1ST SESSION

# H. R. 980

To amend the Internal Revenue Code of 1986 to provide tax relief for the middle class.

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## IN THE HOUSE OF REPRESENTATIVES

FEBRUARY 16, 1995

Mr. GEPHARDT (for himself and Mr. GIBBONS) (both by request) introduced the following bill; which was referred to the Committee on Ways and Means

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## A BILL

To amend the Internal Revenue Code of 1986 to provide tax relief for the middle class.

1       *Be it enacted by the Senate and House of Representa-*  
2       *tives of the United States of America in Congress assembled,*

3       **SECTION 1. SHORT TITLE; AMENDMENT OF 1986 CODE.**

4       (a) SHORT TITLE.—This Act may be cited as the  
5       “Middle-Class Bill of Rights Tax Relief Act of 1995”.

6       (b) AMENDMENT OF 1986 CODE.—Except as other-  
7       wise expressly provided, whenever in this Act an amend-  
8       ment or repeal is expressed in terms of an amendment  
9       to, or repeal of, a section or other provision, the reference

1 shall be considered to be made to a section or other provi-  
 2 sion of the Internal Revenue Code of 1986.

3 (c) TABLE OF CONTENTS.—

Sec. 1. Short title; amendment of 1986 Code.

TITLE I—MIDDLE CLASS TAX RELIEF

Sec. 101. Credit for families with young children.

Sec. 102. Deduction for higher education expenses.

TITLE II—PROVISIONS RELATING TO INDIVIDUAL RETIREMENT  
 PLANS

Subtitle A—Retirement Savings Incentives

PART I—IRA DEDUCTION

Sec. 201. Increase in income limitations.

Sec. 202. Inflation adjustment for deductible amount and income limitations.

Sec. 203. Coordination of IRA deduction limit with elective deferral limit.

PART II—NONDEDUCTIBLE TAX-FREE IRA'S

Sec. 211. Establishment of nondeductible tax-free individual retirement ac-  
 counts.

Subtitle B—Penalty-Free Distributions

Sec. 221. Distributions from certain plans may be used without penalty to pur-  
 chase first homes, to pay higher education or financially dev-  
 astating medical expenses, or by the unemployed.

Sec. 222. Contributions must be held at least 5 years in certain cases.

4 **TITLE I—MIDDLE CLASS TAX**  
 5 **RELIEF**

6 **SEC. 101. CREDIT FOR FAMILIES WITH YOUNG CHILDREN.**

7 (a) IN GENERAL.—Subpart A of part IV of sub-  
 8 chapter A of chapter 1 (relating to nonrefundable personal  
 9 credits) is amended by inserting after section 22 the fol-  
 10 lowing new section:

11 **“SEC. 23. FAMILIES WITH YOUNG CHILDREN.**

12 **“(a) ALLOWANCE OF CREDIT.—**

1           “(1) IN GENERAL.—In the case of an individ-  
 2           ual, there shall be allowed as a credit against the tax  
 3           imposed by this chapter for the taxable year an  
 4           amount equal to \$300 multiplied by the number of  
 5           eligible children of the taxpayer for the taxable year.

6           “(2) INCREASE IN CREDIT.—In the case of tax-  
 7           able years beginning after December 31, 1998, para-  
 8           graph (1) shall be applied by substituting ‘\$500’ for  
 9           ‘\$300’.

10          “(b) LIMITATIONS.—

11           “(1) PHASE-OUT OF CREDIT.—

12           “(A) IN GENERAL.—The amount of the  
 13           credit allowed under subsection (a) shall be re-  
 14           duced (but not below zero) by the amount de-  
 15           termined under subparagraph (B).

16           “(B) AMOUNT OF REDUCTION.—The  
 17           amount determined under this subparagraph  
 18           equals the amount which bears the same ratio  
 19           to the credit (determined without regard to this  
 20           subsection) as—

21                   “(i) the excess of—

22                           “(I) the taxpayer’s adjusted  
 23                           gross income for such taxable year,  
 24                           over

25                           “(II) \$60,000, bears to

1 “(ii) \$15,000.

2 Any amount determined under this subpara-  
3 graph which is not a multiple of \$10 shall be  
4 rounded to the next lowest \$10.

5 “(C) ADJUSTED GROSS INCOME.—For pur-  
6 poses of this paragraph, adjusted gross income  
7 of any taxpayer shall be increased by any  
8 amount excluded from gross income under sec-  
9 tion 911, 931, or 933.

10 “(2) LIMITATION BASED ON AMOUNT OF  
11 TAX.—The credit allowed by subsection (a) for the  
12 taxable year (after the application of paragraph (1))  
13 shall not exceed the excess (if any) of—

14 “(A) the taxpayer’s regular tax liability for  
15 the taxable year reduced by the credits allow-  
16 able against such tax under this subpart (other  
17 than this section) determined without regard to  
18 section 26, over

19 “(B) the sum of—

20 “(i) the taxpayer’s tentative minimum  
21 tax for such taxable year, plus

22 “(ii) the credit allowed for the taxable  
23 year under section 32.

1       “(c) ELIGIBLE CHILD.—For purposes of this section,  
2 the term ‘eligible child’ means any child (as defined in sec-  
3 tion 151(c)(3)) of the taxpayer—

4               “(1) who has not attained age 13 as of the  
5 close of the calendar year in which the taxable year  
6 of the taxpayer begins,

7               “(2) who is a dependent of the taxpayer with  
8 respect to whom the taxpayer is allowed a deduction  
9 under section 151 for such taxable year, and

10              “(3) whose TIN is included on the taxpayer’s  
11 return for such taxable year.

12       “(d) INFLATION ADJUSTMENTS.—In the case of a  
13 taxable year beginning in a calendar year after 1999—

14              “(1) IN GENERAL.—The \$500 and \$60,000  
15 amounts contained in subsections (a)(2) and (b)(2)  
16 shall each be increased by an amount equal to—

17                      “(A) such dollar amount, multiplied by

18                      “(B) the cost-of-living adjustment deter-  
19 mined under section 1(f)(3) for the calendar  
20 year in which the taxable year begins, deter-  
21 mined by substituting ‘calendar year 1998’ for  
22 ‘calendar year 1992’ in subparagraph (B)  
23 thereof.

24              “(2) INCREASE IN PHASEOUT RANGE.—If the  
25 amount applicable under subsection (a) for any tax-

1       able year exceeds \$500, subsection (b)(2)(B) shall be  
2       applied by substituting an amount equal to 30 times  
3       such applicable amount for ‘\$15,000’.

4           “(3) ROUNDING.—If any amount as adjusted  
5       under paragraph (1) is not a multiple of \$100, such  
6       amount shall be rounded to the next lowest multiple  
7       of \$100.

8       “(e) SPECIAL RULES.—

9           “(1) AMOUNT OF CREDIT MAY BE DETERMINED  
10       UNDER TABLES.—The amount of the credit allowed  
11       by this section may be determined under tables pre-  
12       scribed by the Secretary.

13           “(2) CERTAIN OTHER RULES APPLY.—Rules  
14       similar to the rules of subsections (c)(1) (E) and  
15       (F), (d), and (e) of section 32 shall apply for pur-  
16       poses of this section.”

17       (b) CLERICAL AMENDMENT.—The table of sections  
18       for subpart A of part IV of subchapter A of chapter 1  
19       is amended by inserting after the item relating to section  
20       22 the following new item:

          “Sec. 23. Families with young children.”

21       (c) EFFECTIVE DATE.—The amendments made by  
22       this section shall apply to taxable years beginning after  
23       December 31, 1995.

1 **SEC. 102. DEDUCTION FOR HIGHER EDUCATION EXPENSES.**

2 (a) DEDUCTION ALLOWED.— Part VII of subchapter  
3 B of chapter 1 (relating to additional itemized deductions  
4 for individuals) is amended by redesignating section 220  
5 as section 221 and by inserting after section 219 the fol-  
6 lowing new section:

7 **“SEC. 220. HIGHER EDUCATION TUITION AND FEES.**

8 “(a) ALLOWANCE OF DEDUCTION.—In the case of an  
9 individual, there shall be allowed as a deduction the  
10 amount of qualified higher education expenses paid by the  
11 taxpayer during the taxable year.

12 “(b) LIMITATIONS.—

13 “(1) DOLLAR LIMITATION.—

14 “(A) IN GENERAL.—The amount allowed  
15 as a deduction under subparagraph (a) for any  
16 taxable year shall not exceed \$10,000.

17 “(B) PHASE-IN.—In the case of taxable  
18 years beginning in 1996, 1997, or 1998,  
19 ‘\$5,000’ shall be substituted for ‘\$10,000’ in  
20 subparagraph (A).

21 “(2) LIMITATION BASED ON MODIFIED AD-  
22 JUSTED GROSS INCOME.—

23 “(A) IN GENERAL.—The amount which  
24 would (but for this paragraph) be taken into ac-  
25 count under paragraph (1) shall be reduced

(but not below zero) by the amount determined under subparagraph (B).

“(B) AMOUNT OF REDUCTION.—The amount determined under this subparagraph equals the amount which bears the same ratio to the amount which would be so taken into account as—

“(i) the excess of—

“(I) the taxpayer’s modified adjusted gross income for such taxable year, over

“(II) \$70,000 (\$100,000 in the case of a joint return), bears to

“(ii) \$20,000.

“(C) MODIFIED ADJUSTED GROSS INCOME.—The term ‘modified adjusted gross income’ means the adjusted gross income of the taxpayer for the taxable year determined—

“(i) without regard to this section and sections 911, 931, and 933, and

“(ii) after the application of sections 86, 135, 219 and 469.

For purposes of sections 86, 135, 219, and 469, adjusted gross income shall be determined



1 without regard to the deduction allowed under  
2 this section.

3 “(D) INFLATION ADJUSTMENTS.—

4 “(i) IN GENERAL.—In the case of a  
5 taxable year beginning after 1999, the  
6 \$70,000 and \$100,000 amounts described  
7 in subparagraph (B) shall each be in-  
8 creased by an amount equal to—

9 “(I) such dollar amounts, multi-  
10 plied by

11 “(II) the cost-of-living adjust-  
12 ment determined under section 1(f)(3)  
13 for the calendar year in which the tax-  
14 able year begins, determined by sub-  
15 stituting ‘calendar year 1998’ for ‘cal-  
16 endar year 1992’ in subparagraph (B)  
17 thereof.

18 “(ii) ROUNDING.—If any amount as  
19 adjusted under clause (i) is not a multiple  
20 of \$5,000, such amount shall be rounded  
21 to the next lowest multiple of \$5,000.

22 “(c) QUALIFIED HIGHER EDUCATION EXPENSES.—

23 For purposes of this section—

24 “(1) QUALIFIED HIGHER EDUCATION EX-  
25 PENSES.—

1           “(A) IN GENERAL.—The term ‘qualified  
2 higher education expenses’ means tuition and  
3 fees charged by an educational institution and  
4 required for the enrollment or attendance of—

5                   “(i) the taxpayer,

6                   “(ii) the taxpayer’s spouse, or

7                   “(iii) any dependent of the taxpayer  
8 with respect to whom the taxpayer is al-  
9 lowed a deduction under section 151,  
10 as an eligible student at an institution of higher  
11 education.

12           “(B) EXCEPTION FOR EDUCATION INVOLV-  
13 ING SPORTS, ETC.—Such term does not include  
14 expenses with respect to any course or other  
15 education involving sports, games, or hobbies,  
16 unless such expenses—

17                   “(i) are part of a degree program, or

18                   “(ii) are deductible under this chapter  
19 without regard to this section.

20           “(C) EXCEPTION FOR NONACADEMIC  
21 FEES.—Such term does not include any student  
22 activity fees, athletic fees, insurance expenses,  
23 or other expenses unrelated to a student’s aca-  
24 demic course of instruction.

1           “(D) ELIGIBLE STUDENT.—For purposes  
2 of subparagraph (A), the term ‘eligible student’  
3 means a student who—

4           “(i) meets the requirements of section  
5 484(a)(1) of the Higher Education Act of  
6 1965 (20 U.S.C. 1091(a)(1)), as in effect  
7 on the date of the enactment of this sec-  
8 tion, and

9           “(ii)(I) is carrying at least one-half  
10 the normal full-time work load for the  
11 course of study the student is pursuing, as  
12 determined by the institution of higher  
13 education, or

14           “(II) is enrolled in a course which en-  
15 ables the student to improve the student’s  
16 job skills or to acquire new job skills.

17           “(E) IDENTIFICATION REQUIREMENT.—No  
18 deduction shall be allowed under subsection (a)  
19 to a taxpayer with respect to an eligible student  
20 unless the taxpayer includes the name, age, and  
21 taxpayer identification number of such eligible  
22 student on the return of tax for the taxable  
23 year.

1           “(2) INSTITUTION OF HIGHER EDUCATION.—

2           The term ‘institution of higher education’ means an  
3           institution which—

4                   “(A) is described in section 481 of the  
5                   Higher Education Act of 1965 (20 U.S.C.  
6                   1088), as in effect on the date of the enactment  
7                   of this section, and

8                   “(B) is eligible to participate in programs  
9                   under title IV of such Act.

10          “(d) SPECIAL RULES.—

11               “(1) NO DOUBLE BENEFIT.—

12                   “(A) IN GENERAL.—No deduction shall be  
13                   allowed under subsection (a) for qualified high-  
14                   er education expenses with respect to which a  
15                   deduction is allowable to the taxpayer under  
16                   any other provision of this chapter unless the  
17                   taxpayer irrevocably waives his right to the de-  
18                   duction of such expenses under such other pro-  
19                   vision.

20                   “(B) DEPENDENTS.—No deduction shall  
21                   be allowed under subsection (a) to any individ-  
22                   ual with respect to whom a deduction under  
23                   section 151 is allowable to another taxpayer for  
24                   a taxable year beginning in the calendar year in  
25                   which such individual’s taxable year begins.

1           “(C) SAVINGS BOND EXCLUSION.—A de-  
2           duction shall be allowed under subsection (a)  
3           for qualified higher education expenses only to  
4           the extent the amount of such expenses exceeds  
5           the amount excludable under section 135 for  
6           the taxable year.

7           “(2) LIMITATION ON TAXABLE YEAR OF DE-  
8           DUCTION.—

9           “(A) IN GENERAL.—A deduction shall be  
10          allowed under subsection (a) for any taxable  
11          year only to the extent the qualified higher edu-  
12          cation expenses are in connection with enroll-  
13          ment at an institution of higher education dur-  
14          ing the taxable year.

15          “(B) CERTAIN PREPAYMENTS ALLOWED.—  
16          Subparagraph (A) shall not apply to qualified  
17          higher education expenses paid during a taxable  
18          year if such expenses are in connection with an  
19          academic term beginning during such taxable  
20          year or during the 1st 3 months of the next  
21          taxable year.

22          “(3) ADJUSTMENT FOR CERTAIN SCHOLAR-  
23          SHIPS AND VETERANS BENEFITS.—The amount of  
24          qualified higher education expenses otherwise taken  
25          into account under subsection (a) with respect to the

1 education of an individual shall be reduced (before  
2 the application of subsection (b)) by the sum of the  
3 amounts received with respect to such individual for  
4 the taxable year as—

5 “(A) a qualified scholarship which under  
6 section 117 is not includable in gross income,

7 “(B) an educational assistance allowance  
8 under chapter 30, 31, 32, 34, or 35 of title 38,  
9 United States Code, or

10 “(C) a payment (other than a gift, be-  
11 quest, devise, or inheritance within the meaning  
12 of section 102(a)) for educational expenses, or  
13 attributable to enrollment at an eligible edu-  
14 cational institution, which is exempt from in-  
15 come taxation by any law of the United States.

16 “(4) NO DEDUCTION FOR MARRIED INDIVID-  
17 UALS FILING SEPARATE RETURNS.—If the taxpayer  
18 is a married individual (within the meaning of sec-  
19 tion 7703), this section shall apply only if the tax-  
20 payer and the taxpayer’s spouse file a joint return  
21 for the taxable year.

22 “(5) NONRESIDENT ALIENS.—If the taxpayer is  
23 a nonresident alien individual for any portion of the  
24 taxable year, this section shall apply only if such in-  
25 dividual is treated as a resident alien of the United

1 States for purposes of this chapter by reason of an  
2 election under subsection (g) or (h) of section 6013.

3 “(6) REGULATIONS.—The Secretary may pre-  
4 scribe such regulations as may be necessary or ap-  
5 propriate to carry out this section, including regula-  
6 tions requiring recordkeeping and information re-  
7 porting.”

8 (b) DEDUCTION ALLOWED IN COMPUTING AD-  
9 JUSTED GROSS INCOME.—Section 62(a) is amended by in-  
10 serting after paragraph (15) the following new paragraph:

11 “(16) HIGHER EDUCATION TUITION AND  
12 FEES.—The deduction allowed by section 220.”

13 (c) CONFORMING AMENDMENT.—The table of sec-  
14 tions for part VII of subchapter B of chapter 1 is amended  
15 by striking the item relating to section 220 and inserting:

“Sec. 220. Higher education tuition and fees.  
“Sec. 221. Cross reference.”

16 (d) EFFECTIVE DATE.—The amendments made by  
17 this section shall apply to payments made after December  
18 31, 1995.

1 **TITLE II—PROVISIONS RELAT-**  
2 **ING TO INDIVIDUAL RETIRE-**  
3 **MENT PLANS**

4 **Subtitle A—Retirement Savings**  
5 **Incentives**

6 **PART I—IRA DEDUCTION**

7 **SEC. 201. INCREASE IN INCOME LIMITATIONS.**

8 (a) IN GENERAL.—Subparagraph (B) of section  
9 219(g)(3) is amended—

10 (1) by striking “\$40,000” in clause (i) and in-  
11 serting “\$80,000”, and

12 (2) by striking “\$25,000” in clause (ii) and in-  
13 serting “\$50,000”.

14 (b) PHASE-OUT OF LIMITATIONS.—Clause (ii) of sec-  
15 tion 219(g)(2)(A) is amended by striking “\$10,000” and  
16 inserting “an amount equal to 10 times the dollar amount  
17 applicable for the taxable year under subsection  
18 (b)(1)(A)”.

19 (c) EFFECTIVE DATE.—The amendments made by  
20 this section shall apply to taxable years beginning after  
21 December 31, 1995.



1 **SEC. 202. INFLATION ADJUSTMENT FOR DEDUCTIBLE**  
2 **AMOUNT AND INCOME LIMITATIONS.**

3 (a) IN GENERAL.—Section 219 is amended by redес-  
4 ignating subsection (h) as subsection (i) and by inserting  
5 after subsection (g) the following new subsection:

6 “(h) COST-OF-LIVING ADJUSTMENTS.—

7 “(1) IN GENERAL.—In the case of any taxable  
8 year beginning in a calendar year after 1996, each  
9 dollar amount to which this subsection applies shall  
10 be increased by an amount equal to—

11 “(A) such dollar amount, multiplied by

12 “(B) the cost-of-living adjustment deter-  
13 mined under section 1(f)(3) for the calendar  
14 year in which the taxable year begins, deter-  
15 mined by substituting ‘calendar year 1995’ for  
16 ‘calendar year 1992’ in subparagraph (B)  
17 thereof.

18 “(2) DOLLAR AMOUNTS TO WHICH SUBSECTION  
19 APPLIES.—This subsection shall apply to—

20 “(A) the \$2,000 amounts under subsection  
21 (b)(1)(A) and (c), and

22 “(B) the applicable dollar amounts under  
23 subsection (g)(3)(B).

24 “(3) ROUNDING RULES.—

25 “(A) DEDUCTION AMOUNTS.—If any  
26 amount referred to in paragraph (2)(A) as ad-

1           justed under paragraph (1) is not a multiple of  
2           \$500, such amount shall be rounded to the next  
3           lowest multiple of \$500.

4           “(B) APPLICABLE DOLLAR AMOUNTS.—If  
5           any amount referred to in paragraph (2)(B) as  
6           adjusted under paragraph (1) is not a multiple  
7           of \$5,000, such amount shall be rounded to the  
8           next lowest multiple of \$5,000.”

9       (b) CONFORMING AMENDMENTS.—

10           (1) Clause (i) of section 219(c)(2)(A) is amend-  
11       ed to read as follows:

12                   “(i) the sum of \$250 and the dollar  
13                   amount in effect for the taxable year under  
14                   subsection (b)(1)(A), or”.

15           (2) Section 408(a)(1) is amended by striking  
16       “in excess of \$2,000 on behalf of any individual”  
17       and inserting “on behalf of any individual in excess  
18       of the amount in effect for such taxable year under  
19       section 219(b)(1)(A)”.

20           (3) Section 408(b)(2)(B) is amended by strik-  
21       ing “\$2,000” and inserting “the dollar amount in  
22       effect under section 219(b)(1)(A)”.

23           (4) Subparagraph (A) of section 408(d)(5) is  
24       amended by striking “\$2,250” and inserting “the

1 dollar amount in effect for the taxable year under  
2 section 219(c)(2)(A)(i)’’.

3 (5) Section 408(j) is amended by striking  
4 ‘‘\$2,000’’.

5 (c) EFFECTIVE DATE.—The amendments made by  
6 this section shall apply to taxable years beginning after  
7 December 31, 1995.

8 **SEC. 203. COORDINATION OF IRA DEDUCTION LIMIT WITH**  
9 **ELECTIVE DEFERRAL LIMIT.**

10 (a) IN GENERAL.—Section 219(b) (relating to maxi-  
11 mum amount of deduction) is amended by adding at the  
12 end the following new paragraph:

13 ‘‘(4) COORDINATION WITH ELECTIVE DEFER-  
14 RAL LIMIT.—The amount determined under para-  
15 graph (1) or subsection (c)(2) with respect to any  
16 individual for any taxable year shall not exceed the  
17 excess (if any) of—

18 ‘‘(A) the limitation applicable for the tax-  
19 able year under section 402(g)(1), over

20 ‘‘(B) the elective deferrals (as defined in  
21 section 402(g)(3)) of such individual for such  
22 taxable year.’’

23 (b) CONFORMING AMENDMENT.—Section 219(c) is  
24 amended by adding at the end the following new para-  
25 graph:

1 “(3) CROSS REFERENCE.—

“For reduction in paragraph (2) amount, see subsection (b)(4).”

2 (c) EFFECTIVE DATE.—The amendments made by  
3 this section shall apply to taxable years beginning after  
4 December 31, 1995.

## 5 **PART II—NONDEDUCTIBLE TAX-FREE** 6 **IRA’S**

### 7 **SEC. 211. ESTABLISHMENT OF NONDEDUCTIBLE TAX-FREE** 8 **INDIVIDUAL RETIREMENT ACCOUNTS.**

9 (a) IN GENERAL.—Subpart A of part I of subchapter  
10 D of chapter 1 (relating to pension, profit-sharing, stock  
11 bonus plans, etc.) is amended by inserting after section  
12 408 the following new section:

#### 13 **“SEC. 408A. SPECIAL INDIVIDUAL RETIREMENT ACCOUNTS.**

14 “(a) GENERAL RULE.—Except as provided in this  
15 chapter, a special individual retirement account shall be  
16 treated for purposes of this title in the same manner as  
17 an individual retirement plan.

18 “(b) SPECIAL INDIVIDUAL RETIREMENT AC-  
19 COUNT.—For purposes of this title, the term ‘special indi-  
20 vidual retirement account’ means an individual retirement  
21 plan which is designated at the time of establishment of  
22 the plan as a special individual retirement account.

23 “(c) TREATMENT OF CONTRIBUTIONS.—

1           “(1) NO DEDUCTION ALLOWED.—No deduction  
2           shall be allowed under section 219 for a contribution  
3           to a special individual retirement account.

4           “(2) CONTRIBUTION LIMIT.—The aggregate  
5           amount of contributions for any taxable year to all  
6           special individual retirement accounts maintained for  
7           the benefit of an individual shall not exceed the ex-  
8           cess (if any) of—

9                   “(A) the maximum amount allowable as a  
10                  deduction under section 219 with respect to  
11                  such individual for such taxable year, over

12                  “(B) the amount so allowed.

13           “(3) SPECIAL RULES FOR QUALIFIED TRANS-  
14           FERS.—

15                   “(A) IN GENERAL.—No rollover contribu-  
16                  tion may be made to a special individual retire-  
17                  ment account unless it is a qualified transfer.

18                   “(B) LIMIT NOT TO APPLY.—The limita-  
19                  tion under paragraph (2) shall not apply to a  
20                  qualified transfer to a special individual retire-  
21                  ment account.

22           “(d) TAX TREATMENT OF DISTRIBUTIONS.—

23                   “(1) IN GENERAL.—Except as provided in this  
24                  subsection, any amount paid or distributed out of a

1 special individual retirement account shall not be in-  
2 cluded in the gross income of the distributee.

3 “(2) EXCEPTION FOR EARNINGS ON CONTRIBU-  
4 TIONS HELD LESS THAN 5 YEARS.—

5 “(A) IN GENERAL.—Any amount distrib-  
6 uted out of a special individual retirement ac-  
7 count which consists of earnings allocable to  
8 contributions made to the account during the 5-  
9 year period ending on the day before such dis-  
10 tribution shall be included in the gross income  
11 of the distributee for the taxable year in which  
12 the distribution occurs.

13 “(B) ORDERING RULE.—

14 “(i) FIRST-IN, FIRST-OUT RULE.—  
15 Distributions from a special individual re-  
16 tirement account shall be treated as having  
17 been made—

18 “(I) first from the earliest con-  
19 tribution (and earnings allocable  
20 thereto) remaining in the account at  
21 the time of the distribution, and

22 “(II) then from other contribu-  
23 tions (and earnings allocable thereto)  
24 in the order in which made.

1           “(ii) ALLOCATIONS BETWEEN CON-  
 2           TRIBUTIONS AND EARNINGS.—Any portion  
 3           of a distribution allocated to a contribution  
 4           (and earnings allocable thereto) shall be  
 5           treated as allocated first to the earnings  
 6           and then to the contribution.

7           “(iii) ALLOCATION OF EARNINGS.—  
 8           Earnings shall be allocated to a contribu-  
 9           tion in such manner as the Secretary may  
 10          by regulations prescribe.

11          “(iv) CONTRIBUTIONS IN SAME  
 12          YEAR.—Except as provided in regulations,  
 13          all contributions made during the same  
 14          taxable year may be treated as 1 contribu-  
 15          tion for purposes of this subparagraph.

16          “(C) CROSS REFERENCE.—

**“For additional tax for early withdrawal, see sec-  
 tion 72(t).**

17          “(3) QUALIFIED TRANSFER.—

18               “(A) IN GENERAL.—Paragraph (2) shall  
 19               not apply to any distribution which is trans-  
 20               ferred in a qualified transfer to another special  
 21               individual retirement account.

22               “(B) CONTRIBUTION PERIOD.—For pur-  
 23               poses of paragraph (2), the special individual  
 24               retirement account to which any contributions

1 are transferred shall be treated as having held  
2 such contributions during any period such con-  
3 tributions were held (or are treated as held  
4 under this subparagraph) by the special individ-  
5 ual retirement account from which transferred.

6 “(4) SPECIAL RULES RELATING TO CERTAIN  
7 TRANSFERS.—

8 “(A) IN GENERAL.—Notwithstanding any  
9 other provision of law, in the case of a qualified  
10 transfer to a special individual retirement ac-  
11 count from an individual retirement plan which  
12 is not a special individual retirement account—

13 “(i) there shall be included in gross  
14 income any amount which, but for the  
15 qualified transfer, would be includible in  
16 gross income, but

17 “(ii) section 72(t) shall not apply to  
18 such amount.

19 “(B) TIME FOR INCLUSION.—In the case  
20 of any qualified transfer which occurs before  
21 January 1, 1997, any amount includible in  
22 gross income under subparagraph (A) with re-  
23 spect to such contribution shall be includible  
24 ratably over the 4-taxable year period beginning  
25 in the taxable year in which the amount was



1           paid or distributed out of the individual retire-  
2           ment plan.

3           “(e) QUALIFIED TRANSFER.—For purposes of this  
4 section—

5           “(1) IN GENERAL.—The term ‘qualified trans-  
6           fer’ means a transfer to a special individual retire-  
7           ment account from another such account or from an  
8           individual retirement plan but only if such transfer  
9           meets the requirements of section 408(d)(3).

10           “(2) LIMITATION.—A transfer otherwise de-  
11           scribed in paragraph (1) shall not be treated as a  
12           qualified transfer if the taxpayer’s adjusted gross in-  
13           come for the taxable year of the transfer exceeds the  
14           sum of—

15                   “(A) the applicable dollar amount, plus

16                   “(B) the dollar amount applicable for the  
17           taxable year under section 219(g)(2)(A)(ii).

18           This paragraph shall not apply to a transfer from a  
19           special individual retirement account to another spe-  
20           cial individual retirement account.

21           “(3) DEFINITIONS.—For purposes of this sub-  
22           section, the terms ‘adjusted gross income’ and ‘ap-  
23           plicable dollar amount’ have the meanings given  
24           such terms by section 219(g)(3), except subpara-  
25           graph (A)(ii) thereof shall be applied without regard

1 to the phrase ‘or the deduction allowable under this  
2 section’.”

3 (b) EARLY WITHDRAWAL PENALTY.—Section 72(t)  
4 is amended by adding at the end the following new para-  
5 graph:

6 “(6) RULES RELATING TO SPECIAL INDIVIDUAL  
7 RETIREMENT ACCOUNTS.—In the case of a special  
8 individual retirement account under section 408A—

9 “(A) this subsection shall only apply to  
10 distributions out of such account which consist  
11 of earnings allocable to contributions made to  
12 the account during the 5-year period ending on  
13 the day before such distribution, and

14 “(B) paragraph (2)(A)(i) shall not apply to  
15 any distribution described in subparagraph  
16 (A).”

17 (c) EXCESS CONTRIBUTIONS.—Section 4973(b) is  
18 amended by adding at the end the following new sentence:  
19 “For purposes of paragraphs (1)(B) and (2)(C), the  
20 amount allowable as a deduction under section 219 shall  
21 be computed without regard to section 408A.”

22 (d) CONFORMING AMENDMENT.—The table of sec-  
23 tions for subpart A of part I of subchapter D of chapter  
24 1 is amended by inserting after the item relating to section  
25 408 the following new item:

“Sec. 408A. Special individual retirement accounts.”

1 (e) EFFECTIVE DATE.—The amendments made by  
2 this section shall apply to taxable years beginning after  
3 December 31, 1995.

## 4 **Subtitle B—Penalty-Free** 5 **Distributions**

6 **SEC. 221. DISTRIBUTIONS FROM CERTAIN PLANS MAY BE**  
7 **USED WITHOUT PENALTY TO PURCHASE**  
8 **FIRST HOMES, TO PAY HIGHER EDUCATION**  
9 **OR FINANCIALLY DEVASTATING MEDICAL EX-**  
10 **PENSES, OR BY THE UNEMPLOYED.**

11 (a) IN GENERAL.—Paragraph (2) of section 72(t)  
12 (relating to exceptions to 10-percent additional tax on  
13 early distributions from qualified retirement plans) is  
14 amended by adding at the end the following new subpara-  
15 graph:

16 “(D) DISTRIBUTIONS FROM CERTAIN  
17 PLANS FOR FIRST HOME PURCHASES OR EDU-  
18 CATIONAL EXPENSES.—Distributions to an in-  
19 dividual from an individual retirement plan—

20 “(i) which are qualified first-time  
21 homebuyer distributions (as defined in  
22 paragraph (7)); or

23 “(ii) to the extent such distributions  
24 do not exceed the qualified higher edu-

1 cation expenses (as defined in paragraph  
2 (8)) of the taxpayer for the taxable year.”

3 (b) FINANCIALLY DEVASTATING MEDICAL EX-  
4 PENSES.—

5 (1) IN GENERAL.—Section 72(t)(3)(A) is  
6 amended by striking “(B),”.

7 (2) CERTAIN LINEAL DESCENDANTS AND AN-  
8 CESTORS TREATED AS DEPENDENTS AND LONG-  
9 TERM CARE SERVICES TREATED AS MEDICAL  
10 CARE.—Subparagraph (B) of section 72(t)(2) is  
11 amended by striking “medical care” and all that fol-  
12 lows and inserting “medical care determined—

13 “(i) without regard to whether the  
14 employee itemizes deductions for such tax-  
15 able year, and

16 “(ii) in the case of an individual re-  
17 tirement plan—

18 “(I) by treating such employee’s  
19 dependents as including all children,  
20 grandchildren and ancestors of the  
21 employee or such employee’s spouse  
22 and

23 “(II) by treating qualified long-  
24 term care services (as defined in para-

1 graph (9)) as medical care for pur-  
2 poses of this subparagraph (B).”

3 (3) CONFORMING AMENDMENT.—Subparagraph  
4 (B) of section 72(t)(2) is amended by striking “or  
5 (C)” and inserting “, (C) or (D)”.

6 (c) DEFINITIONS.—Section 72(t), as amended by this  
7 Act, is amended by adding at the end the following new  
8 paragraphs:

9 “(7) QUALIFIED FIRST-TIME HOMEBUYER DIS-  
10 TRIBUTIONS.—For purposes of paragraph  
11 (2)(D)(i)—

12 “(A) IN GENERAL.—The term ‘qualified  
13 first-time homebuyer distribution’ means any  
14 payment or distribution received by an individ-  
15 ual to the extent such payment or distribution  
16 is used by the individual before the close of the  
17 60th day after the day on which such payment  
18 or distribution is received to pay qualified ac-  
19 quisition costs with respect to a principal resi-  
20 dence of a first-time homebuyer who is such in-  
21 dividual or the spouse, child (as defined in sec-  
22 tion 151(c)(3)), or grandchild of such individ-  
23 ual.

24 “(B) QUALIFIED ACQUISITION COSTS.—  
25 For purposes of this paragraph, the term

1           ‘qualified acquisition costs’ means the costs of  
2           acquiring, constructing, or reconstructing a res-  
3           idence. Such term includes any usual or reason-  
4           able settlement, financing, or other closing  
5           costs.

6           “(C) FIRST-TIME HOMEBUYER; OTHER  
7           DEFINITIONS.—For purposes of this paragraph:

8           “(i) FIRST-TIME HOMEBUYER.—The  
9           term ‘first-time homebuyer’ means any in-  
10          dividual if—

11          “(I) such individual (and if mar-  
12          ried, such individual’s spouse) had no  
13          present ownership interest in a prin-  
14          cipal residence during the 3-year pe-  
15          riod ending on the date of acquisition  
16          of the principal residence to which  
17          this paragraph applies, and

18          “(II) subsection (h) or (k) of sec-  
19          tion 1034 did not suspend the run-  
20          ning of any period of time specified in  
21          section 1034 with respect to such in-  
22          dividual on the day before the date  
23          the distribution is applied pursuant to  
24          subparagraph (A).

1 In the case of an individual described in  
2 section 143(i)(1)(C) for any year, an own-  
3 ership interest shall not include any inter-  
4 est under a contract of deed described in  
5 such section. An individual who loses an  
6 ownership interest in a principal residence  
7 incident to a divorce or legal separation is  
8 deemed for purposes of this subparagraph  
9 to have had no ownership interest in such  
10 principal residence within the period re-  
11 ferred to in subparagraph (A)(II).

12 “(ii) PRINCIPAL RESIDENCE.—The  
13 term ‘principal residence’ has the same  
14 meaning as when used in section 1034.

15 “(iii) DATE OF ACQUISITION.—The  
16 term ‘date of acquisition’ means the date—

17 “(I) on which a binding contract  
18 to acquire the principal residence to  
19 which subparagraph (A) applies is en-  
20 tered into, or

21 “(II) on which construction or re-  
22 construction of such a principal resi-  
23 dence is commenced.

24 “(D) SPECIAL RULE WHERE DELAY IN AC-  
25 QUISSION.—If any distribution from any indi-

vidual retirement plan fails to meet the requirements of subparagraph (A) solely by reason of a delay or cancellation of the purchase or construction of the residence, the amount of the distribution may be contributed to an individual retirement plan as provided in section 408(d)(3)(A)(i) (determined by substituting ‘120 days’ for ‘60 days’ in such section), except that—

“(i) section 408(d)(3)(B) shall not be applied to such contribution, and

“(ii) such amount shall not be taken into account in determining whether section 408(d)(3)(A)(i) applies to any other amount.

“(8) QUALIFIED HIGHER EDUCATION EXPENSES.—For purposes of paragraph (2)(D)(ii):

“(A) IN GENERAL.—The term ‘qualified higher education expenses’ means tuition and fees required for the enrollment or attendance of—

“(i) the taxpayer,

“(ii) the taxpayer’s spouse,



1           “(iii) a dependent of the taxpayer  
2           with respect to whom the taxpayer is al-  
3           lowed a deduction under section 151, or

4           “(iv) the taxpayer’s child (as defined  
5           in section 151(c)(3)) or grandchild,  
6           as an eligible student at an institution of higher  
7           education (as defined in paragraphs (1)(D) and  
8           (2) of section 220(c)).

9           “(B) EXCEPTIONS.—The term ‘qualified  
10          higher education expenses’ does not include ex-  
11          penses described in subparagraphs (B) and (C)  
12          of section 220(c)(1).

13          “(C) COORDINATION WITH SAVINGS BOND  
14          PROVISIONS.—The amount of qualified higher  
15          education expenses for any taxable year shall be  
16          reduced by any amount excludable from gross  
17          income under section 135.

18          “(9) QUALIFIED LONG-TERM CARE SERVICES.—  
19          For purposes of paragraph (2)(B)—

20               “(A) IN GENERAL.—The term ‘qualified  
21          long-term care services’ means necessary diag-  
22          nostic, curing, mitigating, treating, preventive,  
23          therapeutic, and rehabilitative services, and  
24          maintenance and personal care services (wheth-

er performed in a residential or nonresidential setting) which—

“(i) are required by an individual during any period the individual is an incapacitated individual (as defined in subparagraph (B)),

“(ii) have as their primary purpose—

“(I) the provision of needed assistance with 1 or more activities of daily living (as defined in subparagraph (C)), or

“(II) protection from threats to health and safety due to severe cognitive impairment, and

“(iii) are provided pursuant to a continuing plan of care prescribed by a licensed professional (as defined in subparagraph (D)).

“(B) INCAPACITATED INDIVIDUAL.—The term ‘incapacitated individual’ means any individual who—

“(i) is unable to perform, without substantial assistance from another individual (including assistance involving cueing or substantial supervision), at least 2 activi-

1           ties of daily living as defined in subpara-  
2           graph (C), or

3           “(ii) has severe cognitive impairment  
4           as defined by the Secretary in consultation  
5           with the Secretary of Health and Human  
6           Services.

7           Such term shall not include any individual oth-  
8           erwise meeting the requirements of the preced-  
9           ing sentence unless a licensed professional with-  
10          in the preceding 12-month period has certified  
11          that such individual meets such requirements.

12          “(C) ACTIVITIES OF DAILY LIVING.—Each  
13          of the following is an activity of daily living:

14               “(i) Eating.

15               “(ii) Toileting.

16               “(iii) Transferring.

17               “(iv) Bathing.

18               “(v) Dressing.

19          “(D) LICENSED PROFESSIONAL.—The  
20          term ‘licensed professional’ means—

21               “(i) a physician or registered profes-  
22               sional nurse, or

23               “(ii) any other individual who meets  
24               such requirements as may be prescribed by

1 the Secretary after consultation with the  
2 Secretary of Health and Human Services.

3 “(E) CERTAIN SERVICES NOT IN-  
4 CLUDED.—The term ‘qualified long-term care  
5 services’ shall not include any services provided  
6 to an individual—

7 “(i) by a relative (directly or through  
8 a partnership, corporation, or other entity)  
9 unless the relative is a licensed professional  
10 with respect to such services, or

11 “(ii) by a corporation or partnership  
12 which is related (within the meaning of  
13 section 267(b) or 707(b)) to the individual.

14 For purposes of this subparagraph, the term  
15 ‘relative’ means an individual bearing a rela-  
16 tionship to the individual which is described in  
17 paragraphs (1) through (8) of section 152(a).”

18 (d) PENALTY-FREE DISTRIBUTIONS FOR CERTAIN  
19 UNEMPLOYED INDIVIDUALS.—Paragraph (2) of section  
20 72(t) is amended by adding at the end the following new  
21 subparagraph:

22 “(E) DISTRIBUTIONS TO UNEMPLOYED IN-  
23 DIVIDUALS.—A distribution from an individual  
24 retirement plan to an individual after separa-  
25 tion from employment, if—

1           “(i) such individual has received un-  
2           employment compensation for 12 consecu-  
3           tive weeks under any Federal or State un-  
4           employment compensation law by reason of  
5           such separation, and

6           “(ii) such distributions are made dur-  
7           ing any taxable year during which such un-  
8           employment compensation is paid or the  
9           succeeding taxable year.”

10       (e) EFFECTIVE DATE.—The amendments made by  
11       this section shall apply to payments and distributions after  
12       December 31, 1995.

13       **SEC. 222. CONTRIBUTIONS MUST BE HELD AT LEAST 5**  
14               **YEARS IN CERTAIN CASES.**

15       (a) IN GENERAL.—Section 72(t), as amended by this  
16       Act, is amended by adding at the end the following new  
17       paragraph:

18               “(10) CERTAIN CONTRIBUTIONS MUST BE HELD  
19       5 YEARS.—

20               “(A) IN GENERAL.—Paragraph (2)(A)(i)  
21       shall not apply to any amount distributed out  
22       of an individual retirement plan (other than a  
23       special individual retirement account) which is  
24       allocable to contributions made to the plan dur-  
25       ing the 5-year period ending on the date of

1 such distribution (and earnings on such con-  
2 tributions).

3 “(B) ORDERING RULE.—For purposes of  
4 this paragraph, distributions shall be treated as  
5 having been made—

6 “(i) first from the earliest contribu-  
7 tion (and earnings allocable thereto) re-  
8 maining in the account at the time of the  
9 distribution, and

10 “(ii) then from other contributions  
11 (and earnings allocable thereto) in the  
12 order in which made.

13 Earnings shall be allocated to contributions in  
14 such manner as the Secretary may prescribe.

15 “(C) SPECIAL RULE FOR ROLLOVERS.—

16 “(i) PENSION PLANS.—Subparagraph  
17 (A) shall not apply to distributions out of  
18 an individual retirement plan which are al-  
19 locable to rollover contributions to which  
20 section 402(c), 403(a)(4), or 403(b)(8) ap-  
21 plied.

22 “(ii) CONTRIBUTION PERIOD.—For  
23 purposes of subparagraph (A), amounts  
24 shall be treated as having been held by a  
25 plan during any period such contributions

1           were held (or are treated as held under  
2           this clause) by any individual retirement  
3           plan from which transferred.

4           “(D) SPECIAL ACCOUNTS.—For rules ap-  
5           plicable to special individual retirement ac-  
6           counts under section 408A, see paragraph (8).”

7           (b) EFFECTIVE DATE.—The amendment made by  
8           this section shall apply to contributions (and earnings allo-  
9           cable thereto) which are made after December 31, 1995.

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HR 980 IH——2

HR 980 IH——3

HR 980 IH——4